

**STATE OF MICHIGAN
DEPARTMENT OF CONSUMER AND INDUSTRY SERVICES
OFFICE OF FINANCIAL AND INSURANCE SERVICES**

Before the Commissioner of Financial and Insurance Services

**In the Matter of Conforming
Insurance Credit Scoring Practices
With Insurance Code Requirements**

Order No. 03-005-M

**Issued and entered
this 14th day of February 2003
by Frank M. Fitzgerald
Commissioner**

**ORDER TO MONITOR INSURER PRACTICES AND
TO INITIATE COMPLIANCE ACTIONS AS APPROPRIATE**

**I
BACKGROUND**

Insurance credit scoring is used by insurers to rate and underwrite coverage. They have found that a person's credit history is a good predictor of whether the person will file insurance claims. Credit history includes such items as bankruptcy, late payments on loans, and the use of credit cards. Based on that history, a score is developed.

In Michigan, insurers are limited in the use of insurance credit scoring with respect to automobile and homeowners insurance. They may only use it to set premiums, not to underwrite. However, they may use it in both rating and underwriting of other personal lines insurance, such as insurance on mobile homes and recreational vehicles.

Policyholders and consumer advocacy groups have expressed concern over the use of insurance credit scoring. Unlike seat belts and fire alarms, there is no obvious reason why a good credit history leads to lower losses. Moreover, some persons believe

the use of insurance credit scoring unfairly discriminates against minorities, the young, and the elderly.

To look into these and other issues, the Commissioner of the Office of Financial and Insurance Services ("OFIS") conducted six public hearings throughout the state last summer. Input from interest groups was sought and received. Major insurers were required to answer detailed inquiries. Credit scoring formulas and factors used in those formulas were obtained. Actuarial studies were taken into account.

II ANALYSIS

In December, the Commissioner issued a report (the "Report") entitled, "The Use of Insurance Credit Scoring in Automobile and Homeowners Insurance." The Report contains a detailed explanation of the use of insurance credit scoring and an analysis of its impact and legality. The Report is attached to this Order and incorporated by reference.

Highlights from the Report include the following:

- The use of insurance credit scoring in the rating of automobile and homeowners insurance is widespread.
- Using insurance credit scoring to discount automobile and homeowners insurance rates is lawful.
- In general, a person with a good credit history is less likely to file automobile or homeowners insurance claims than a person with a bad credit history.
- Independent studies should be undertaken to establish whether insurance credit scoring results in unfair or prohibited discrimination.

- Legislation is recommended to enhance consumer protection, including improved notification to consumers, restrictions against underwriting by use of insurance credit scoring in certain lines of insurance, and prohibitions on the consideration of certain factors in a credit history.
- Many insurance companies are failing to adhere to requirements in Michigan and federal law in their use of insurance credit scoring.

The purpose of this Order is to direct the Staff of OFIS to undertake certain actions to secure compliance with Michigan and federal law.

III FINDINGS OF FACT

Based upon information underlying the Report, it is found that:

1. Several insurance companies have not done the following: (a) filed with OFIS the formula they use to apply credit scoring discounts; (b) filed factors used to calculate an insurance credit score; (c) recalculated and applied discounts at least once annually; (d) filed actuarial certifications justifying discount levels and discount tiers; (e) actuarially certified discounts granted where there is no or little credit history; (f) filed comparable materials to those listed above with respect to personal lines insurance other than automobile and homeowners insurance; (g) annually informed their automobile and homeowners policyholders of the credit score used; (h) recalculated premiums where an insured has successfully disputed credit history information; and, (i) have not advised

applicants and policyholders of adverse actions caused by the application of an insurance credit score.

2. Distribution of the attached bulletin, diligent monitoring of insurer conduct, and bringing appropriate enforcement actions will achieve substantial compliance by insurers with Michigan and federal laws in their insurance credit scoring practices.

IV CONCLUSIONS OF LAW

Based upon a review of the applicable laws cited and discussed in the Report, and particularly with reference to the section in the Report entitled, "Compliance with the Insurance Code," it is concluded that:

1. The actions and inactions of some insurers in their use of credit insurance scoring are in violation of Michigan and federal laws.
2. The Commissioner is authorized to investigate the conduct of insurers and to bring enforcement actions against them as warranted.

V ORDER

Therefore, it is ORDERED that the Staff shall promptly distribute the attached bulletin to affected companies, diligently monitor company compliance with the directives set forth in the bulletin, and initiate compliance actions as appropriate based upon laws underlying the directives that are identified and discussed in the Report.

Frank M. Fitzgerald
Commissioner